

Message Text

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ACTION NEA-10

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E.O. 11652: N/A
TAGS: ECON, IS
SUBJECT: BOI GOVERNOR GAFNI DISCUSSES ISRAELI ECONOMY

REF: TEL AVIV 571

1. SUMMARY: BANK OF ISRAEL GOVERNOR ARNON GAFNI IS CAUTIOUSLY OPTIMISTIC ABOUT LONGER-TERM ECONOMIC PROSPECTS BUT IS CONCERNED ABOUT WAGE AND PRICE SITUATION OVER THE NEXT FEW MONTHS. HE STRESSES THAT THE DESIRED RESUMPTION OF ECONOMIC GROWTH MUST BE EXPORT-LED, WHICH IS IN TURN DEPENDENT ON GREATER SUCCESS IN CURBING INFLATION. END SUMMARY.

2. BANK OF ISRAEL GOVERNOR GAFNI ADDRESSED FOREIGN COMMERCIAL AND ECONOMIC OFFICERS JANUARY 27. TALKING FREELY ON SUCCESSES AND FAILURES IN RECENT ISRAEL ECONOMIC PERFORMANCE, GAFNI STRESSED THAT CONTINUED IMPROVEMENT IN THE BALANCE OF PAYMENTS REMAINS ISRAEL'S MAJOR ECONOMIC GOAL. AMELIORATION OF BOP IS FINALLY APPEARING FOLLOWING GOVERNMENT EFFORTS OF PAST THREE YEARS. WITH IMPORTS A FUNCTION OF OVERALL DEMAND, THE GOI HAD
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FOLLOWED A POLICY OF DEMAND RESTRAINT, HOLDING CONSUMPTION AT 1974 LEVELS AND SLOWING THE RAPID RISE IN PUBLIC SECTOR SPENDING EXCEPT FOR DEBT SERVICE PAYMENTS. EXPORTS, WHILE PARTLY A FUNCTION OF FOREIGN DEMAND, ALSO BENEFITED FROM RESTRAINTS ON INTERNAL DEMAND AND DEVALUATION POLICIES OF GOI. EXPECTATIONS OF GOI POLICY BY PRIVATE SECTOR HAD FINALLY CHANGED SO THAT MANUFACTUR-

ERS NOW UNDERSTAND THAT PRODUCING DIRECTLY FOR EXPORT
WILL BE MORE PROFITABLE THAN PRODUCING FOR LOCAL MARKET.

3. THE NEAR-ZERO GROWTH IN GNP OVER THE LAST TWO YEARS,
AFTER PRE-1973 RECORD OF 10 PERCENT ANNUAL GROWTH, IS A
MAJOR PROBLEM. THE DIFFICULTY IS THAT BY ENCOURAGING
GROWTH THROUGH CONSUMPTION-LED OR GOVERNMENT-LED SPEND-
ING, BOP PROBLEMS CAN BE QUICKLY EXACERBATED. THEREFORE,
GROWTH HAD TO BE EXPORT LED, THROUGH THE BOP SECTOR OF
THE GNP ACCOUNTS.

4. ON PRICE FRONT, GAFNI CONCEDED THAT MISTAKES HAD
BEEN MADE WHEREBY CERTAIN SECTORS HAD RECEIVED HIGH
WAGE INCREASES. HE NOW THOUGHT THE MAIN DANGER WAS IN
A POSSIBLE SECOND ROUND OF WAGE INCREASES AS OTHER MAJOR GROUPS,
INCLUDING THOSE IN PRIVATE SECTOR, TRIED TO CATCH UP.
A SECOND WAVE OF WAGE INCREASES COULD ADD 5 TO 10 PER
CENT BY BOI ESTIMATES TO THE 1977 INFLATION RATE, WHICH
IS ALREADY FIGURED AT A MINIMUM 25 PERCENT LEVEL.

5. GAFNI EMPHASIZED THAT ESSENTIAL TO THE BUDGET AND TO
THE ECONOMIC FORECAST IS A PACKAGE WAGE-PRICE DEAL IN-
VOLVING THE GOI, LABOR, AND EMPLOYERS. PACKAGE IDEALLY
SHOULD BE CONFIRMED BY LEGISLATION; HOWEVER, IMPLICIT
DEAL ARRANGED SO THAT EACH SECTOR BEHAVED WITH RESTRAINT
MIGHT PERMIT ECONOMIC GOALS TO BE MET.

6. WITH REGARD TO SIZE OF 1977 BUDGET, HE EXPRESSED
HIS PERSONAL VIEW THAT IT SHOULD BE CUT BY IL 2 BILLION.
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HE NOTED THAT GOVERNMENT HAD IN FACT PROPOSED TO SPEND
IL 2 BILLION LESS THAN PRORATED AMOUNT OVER FIRST SIX
MONTHS OF FISCAL YEAR. HE THOUGHT THAT THIS SHOULD BE
DONE AND THIS AMOUNT THEN DEDUCTED FROM BUDGET FOR
ENTIRE YEAR.

7. COMMENT: GAFNI'S REMARKS ON NECESSITY OF PACKAGE
DEAL CONTRAST SHARPLY WITH STATEMENT BY FINANCE MINISTER
RABINOWITZ THAT BUDGET STANDS ON ITS OWN REGARDLESS OF
OUTCOME OF GOI-LABOR-EMPLOYER NEGOTIATIONS (SEE REFTTEL).
IF RABINOWITZ IS CORRECT IN PREDICTING THAT AN AGREEMENT
FOR AVOIDING A "SECOND WAVE" OF WAGE INCREASES ARE
BLEAK INDEED.
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Message Attributes

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